ALJ/EA/hh

Decision No. 92178 SEP 3 - 1980

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the matter of the application of ARROWHEAD MANOR WATER COMPANY, a California corporation, for authority to execute a loan contract with the State Department of Water Resources for a $884,000 loan and to increase rates for water service.	Application No. 57533 (Filed August 23, 1977; amended May 21, 1979 and May 29, 1979)

Additional Appearances

Jeffrey L. Stone, for the State Department of Health, interested party.
Robert M. Mann, for the Commission staff.

O P I N I O N

General

Arrowhead Manor Water Company, Inc. (applicant), a California corporation, provides water service to 545 flat rate and 46 metered customers within and adjacent to the unincorporated community of Cedar Glen, a mountain resort area which is located approximately one mile southeast of Lake Arrowhead in San Bernardino County.

Applicant's water system, created by the interconnection of two separate systems in 1957, is supplied water from a tunnel diversion, a horizontal well, and from connections to the Crestline-Lake Arrowhead Water Agency (CLAWA). There is a variation of elevations within the service area in excess of 400 feet. Applicant and/or its predecessors have installed several steel tanks, a hydropneumatic tank, and booster pumps to provide water service. The bulk of the mains in the system are substandard and undersized. Applicant's system requires greater transmission capacity, additional storage, and additional sources of water to meet the needs of its customers.

Applicant seeks Commission authority to: (a) enter into a $910,520[1] loan agreement, under the Safe Drinking Water Bond Act of 1976, with the Department of Water Resources (DWR); (b) use the loan proceeds to pay for the installation of system improvements; and (c) establish annual surcharges, payable on a prorated basis, to amortize the principal and to make 5.5 percent[2] interest payments on the loan over 35 years.

The revenue to meet the semiannual payments on the SDWBA loan will be obtained from surcharges on all metered and flat-rate services. The total amount of revenue from the proposed surcharge will exceed the loan repayment requirements by approximately 10 percent. In accordance with DWR requirements, this overcollection will be deposited with the fiscal agent to accumulate a reserve equal to two semiannual loan payments over a 10-year period. Earnings of the reserve fund, net of charges for the fiscal agent's services, will be added to the fund. Net earnings of the reserve fund will be used, together with surcharge amounts collected from customers, to meet the semiannual loan payments. The Commission reserves the right to review the manner in which the fund is invested and to direct that a different fiscal agent acceptable to DWR be selected, if appropriate.

The annual requirements for debt service will be approximately $64,691. The amount of the surcharge to repay principal, interest, and necessary reserve on the loan will be in direct proportion to the capacity of each customer's meter or service connection. The following surcharge would produce approximately $5,391 per month, requiring an increase in water rates of approximately $9.08 per month for each residential customer.

1/ This amount contained in the amended application added $26,520 for a 3 percent DWR administrative fee.

2/ DWR may be required to modify the interest rate based upon its bond issuance costs.

Rates

Applicant requests authorization of the following initial annual surcharges to pay off the DWR loan:

Size of Meter or Size of Service	Annual Surcharge[c]
Residential[a]	$ 99.60
3/4-inch meter[b]	149.40
1-inch meter[b]	249.00
1½-inch meter[b]	498.00
2-inch meter[b]	796.00

a/ For service through a 5/8 x 3/4-inch meter or a 3/4-inch service.

b/ Applicable to metered service only.

c/ This surcharge is in addition to regular charges for water service. After the system has been fully metered, the surcharge may be based on water usage.

To meet the 10 percent reserve requirement imposed by DWR Administrative Regulations it will be necessary to revise the annual surcharges proposed by applicant to the following amounts:

Size of Meter or Size of Service	Annual Surcharge[c]
Residential[a]	$109.00
3/4-inch meter[b]	163.50
1-inch meter[b]	272.50
1½-inch meter[b]	545.00
2-inch meter[b]	872.00

a/ For service through a 5/8 x 3/4-inch meter or a 3/4-inch service.

b/ Applicable to metered service only.

c/ This surcharge is in addition to regular charges for water service. After the system has been fully metered, the surcharge may be based on water usage.

Summary of Decision

This decision authorizes applicant to enter into a loan agreement with DWR and to establish the annual rate surcharges tabulated above. The surcharges will yield additional annual revenues of $64,691, a 112 percent increase. Applicant may prorate its billings on a bimonthly or quarterly basis.

The funds derived from this loan are needed to construct Phase I of the three-phase improvement plan, which will (a) provide an adequately sized backbone transmission system; (b) eliminate or improve low pressure conditions; (c) provide an adequate water supply and storage to meet the needs of its existing customers and to provide a margin for growth; (d) provide water to meet direct fire protection requirements adjacent to the new facilities in the heavily forested service area; (e) improve fire protection in areas not directly accessible to the new facilities; (f) eliminate some potential backflow hazards, including replacement of a badly deteriorated main on Hook Creek Road; and (g) provide the core facilities needed for Phases II and III.

The facilities proposed to be constructed with the loan funds constitute only a portion of the mains, services, fire hydrants, and meters originally proposed to be constructed with the proceeds of the requested loan. The revised design increased the capacity of supply from CLAWA and the size of portions of the backbone transmission system to meet domestic and fire-flow requirements from the new mains.[3/]

Absent this authorization, applicant, which cannot obtain funds for construction from conventional lenders[4/] or from its owners, is faced with the rescission of the $15,630 rate

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3/ In the original two-phase plan both phases would have to be completed to provide required fire flow from all new hydrants.

4/ Originally contemplated interim financing for the Hook Creek Road improvement is not available at this time. DWR is loaning money for future construction.

increase authorized in D.90877.[5] Applicant's consultants believe that there will be more leaks in the future if the main replacement program does not commence. Applicant's consultants also testified that operating funds available to applicant only sufficed to patch leaks or to replace short sections of undersized mains. Applicant's customers also described frequent breaks and hazards from leaky mains (e.g., the formation of ice on roadways).

A cash flow of $10,000 is insufficient to arrest further deterioration of applicant's system. A rate reduction would exacerbate the deterioration in service.

Notice and Public Hearings

Pursuant to the ruling of Administrative Law Judge Levander (ALJ), applicant's customers were mailed copies of a notice (Reference Item H herein) setting forth (a) applicant's estimate of $2,540,000 to construct the three-phase program, excluding inflation, contingencies, and overhead costs; (b) applicant's Phase I construction cost estimate of $585,000 which, with the inclusion of all associated costs, would require the entire proceeds of the $910,520 loan; (c) a tabulation of applicant's proposed surcharges[6] which were "to be used only for repayment of principal and interest on the $910,520 loan"; (d) a statement that applicant had prepared a preliminary engineering report, which was available for inspection at applicant's office, and that "no scheduling has been proposed for construction or financing

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5/ D.90877 states: "This rate increase shall be rescinded on August 1, 1980 if the Hook Creek Road improvement has not been completed by July 31, 1980."

6/ A footnote error in the notice overstated the requested annual surcharges for 5/8-inch x 3/4-inch metered services and for 3/4-inch services at $149.40 rather than the $99.60 requested.

of the remaining facilities (Phases II and III)"; and (e) a statement notifying customers that they could submit comments on applicant's proposal or request a hearing notice by writing to Robert Mann of the Commission staff.

After notice by publication, posting, and mailings to customers, hearings were held in the cities of San Bernardino and Los Angeles on February 28 and 29, 1980. The matter was submitted subject to the filing of late-filed exhibits by March 7, 1980, and to the filing of a staff brief by March 20, 1980. The late-filed exhibits and brief have been received.

Public Comments

Exhibit 10 contains a list of 11 customers responding to Reference Item H. All of the letters protested the increase. The staff believes that the addresses of these 11 customers indicate that none of them permanently resides in the service territory.

At the hearing, five customers commented on the application. They questioned (a) the magnitude of the increase; (b) their ability to pay either as retirees on fixed incomes or for a second home with limited use; (c) the fairness of paying for replacements which should have been made in the past (e.g., there should have been a main replacement where numerous closely spaced leaks in a badly corroded pipe created a hazard); (d) the impact of higher pressures on old customer-owned plumbing; (e) the higher surcharge on metered customers (see footnote 6); and (f) unserviceable fire hydrants. One customer questioned whether the priorities of the Lake Arrowhead Fire Protection District (FPD) would result in protecting the forest rather than homes.

Original Plans

Applicant originally anticipated that the loan proceeds would pay for (a) an engineering master plan; (b) replacement of approximately one-half of its water mains,[7] most of which are less than two inches in diameter, with 49,780 feet of 6-inch diameter and 3,270 feet of 8-inch diameter mains; (c) rehabilitation of a 50,000-gallon water storage tank and the purchase of a 250,000-gallon tank; (d) installation of a hydropneumatic pressure system to eliminate low pressures near storage facilities; (e) two connections to CLAWA's system; (f) water conservation measures, including the installation of 600 meters; (g) replacement of 470 services; and (h) installation of 89 fire hydrants. The initial two-phase construction cost estimates were based upon 1977 cost levels.

Revisions in Proposed Construction

Applicant engaged a consulting engineering firm shortly before the initial hearings in this proceeding. Late-filed Exhibits 5-1 and 5-2 contain the consultants' revised predesign cost estimate of $1,754,900 to complete applicant's proposed two-phase, two-year construction program. Under this plan 320 customers would have been served from new Phase I facilities, 100 customers would be served from new Phase II facilities, and 120 customers would not be directly served from new facilities. Since applicant proposed to borrow $910,520 from DWR, the scope of applicant's proposal was unclear.

D.90877 dated October 10, 1979 in A.58868: (a) authorized a contingent general rate increase (see footnote 5); (b) required applicant to inform the Commission of its intent to proceed with the instant application; and (c) required applicant to provide additional information required for this Commission's evaluation of applicant's proposal if it elected to proceed. Applicant

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7/ Applicant's 1979 Annual Report shows a total of 106,136 feet of pipe in applicant's system. Plate 4 of Exhibit 9 shows extensive lengths of unused mains.

indicated its intent to proceed and submitted a preliminary engineering report (Exhibit 8) for a modified three-phase project which contained engineering and cost information. Pursuant to a ruling by the ALJ, applicant submitted an addendum (Exhibit 9) focused on the Phase I construction and supplied information required by D.90877. The reports contain maps showing existing and proposed construction.

Applicant posted maps showing contemplated improvements at its office and made its engineering report available for customer review. Applicant's owner and its consultants discussed the plan with customers and submitted copies for review by the Commission, the State Department of Health (HD) for DWR, and to the FPD.

In its earlier proposal applicant planned to construct portions of its transmission system using 6-inch mains (Phase I) and to construct parallel 6-inch mains in adjacent streets together with interconnections in the following year (Phase II) to meet fire-flow and domestic requirements on the new system.

Since applicant scaled down its Phase I construction plan to avoid increasing the requested surcharges to a level it deemed unacceptable,[8/] applicant did not attempt to schedule dates for Phases II or III construction. Applicant's internally generated funds from operations are not significant compared to the cost of construction. In order to meet fire-flow and domestic requirements in the new Phase I system applicant increased main sizes from six inches to eight inches in its proposed backbone transmission line, except for two 6-inch mains

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8/ Applicant's owners discussed the level of surcharges with its customers and decided not to seek a surcharge higher than the proposed level of approximately $100 per year. Applicant believes that its customers would prefer to pay surcharges on a quarterly or bimonthly basis rather than on an annual basis.

terminating at storage tanks. In response to FPD's suggestions to improve the system's usefulness for fire protection purposes applicant changed the location of certain mains to allow for faster and easier access to hydrants by fire trucks and plans to add a valve for FPD use at each of its storage tanks.

In Phase I applicant proposes to: (a) install approximately 1,350 feet of 6-inch main and 11,810 feet of 8-inch main; (b) connect 22 fire hydrants to the new mains and install outlets for fire protection purposes at its storage tanks; (c) connect 125 customer services[9/] to the new mains; (d) relocate a 125,000-gallon tank; (e) purchase and use a 250,000-gallon tank; (f) rehabilitate an existing 50,000-gallon tank; (g) install three pressure-reducing stations; (h) increase the size of an existing CLAWA connection from 100 gpm to 400 gpm; and (i) construct a new 250 gpm CLAWA connection. The engineering plan would change pressure zones, eliminate constraints preventing greater use of applicant's own sources of supply, and improve to 30 psi, but not eliminate, low pressure conditions. A further improvement eliminating low pressures in the upper portion of its service area would require creation of a new pressure zone fed from a $90,000 hydropneumatic booster station facility.

Applicant's consultants testified that it was prudent to estimate the Phase I costs conservatively based upon their experience in the local mountainous terrain, the limited construction season, and high inflation rates to be sure that all of the facilities could be constructed. The total estimate of $910,520 includes construction costs, based upon the October 1979 Engineering News Record Cost Index for Los Angeles, of $585,000. To the extent that lower than anticipated bids were received, applicant would construct a portion of the Phase II facilities with the remaining funds - including, if possible, the hydropneumatic installation.

9/ Exhibit 8 shows 159 new service connections in Phase I. The map showing the current Phase I proposal is designated as Exhibit 8-2.

Applicant's consultants testified that: (a) direct adequate fire flows would be available to 180 customers from the new fire hydrants; (b) FPD pumper units could string water hoses and boost water to extend the area served from the new hydrants; (c) installation of the hydrants along the backbone system and valves threaded for fire-fighting hoses to applicant's storage tanks would permit more rapid and more frequent movements of tanker trucks for fighting fires in areas not accessible from the new hydrants and fire valves; (d) customers located on the old system would benefit from more adequate water supplies from added storage and new supplies; and (e) applicant's customers, including customers served from old mains, would receive water at higher pressures during periods of heavy demand[10/] than before because there would be less of a pressure loss in the new transmission mains than in the mains replaced.

Construction Required - Applicant's Position

Applicant's consultants testified that: (a) the three-phase plan was designed in good faith and they expected future water system construction perhaps by 1985; (b) increasing the amount of the loan to DWR's limit of $1,500,000 to construct more facilities would be too burdensome to applicant's customers at this time; (c) there was a building moratorium due to the lack of a sewer system in the service area; (d) pressures were building to set up an improvement district to install sewers

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10/ Some customers were concerned that excessive pressures, which could damage their own old piping, would result because of the main replacements. Maximum pressures would occur during periods of low demand, e.g., late in the evening. At that time, pressures would be governed by the water level in applicant's storage tanks (or by the settings of the future hydropneumatic tank), not by the main replacement program.

in the service area (e.g., the residential locations shown on plate 3 of Exhibit 8 and plate 4 of Exhibit 9 were obtained from a sewer study) to remove the moratorium; (e) sewer construction costs would be more costly than the contemplated water system costs; (f) they anticipated a lifting of the building moratorium by 1985 and the addition of 23 customers per year from 1985 to 2000; (g) their estimated growth rate was lower than that made by the San Bernardino County Planning Department because they believed that many unpaved roads in the service area would retard growth slightly; (h) there was a possibility of developers acquiring blocks of some of the 4,300 lots in the service area and resubdividing the land which could provide a source of funds for Phase II or Phase III improvements as advances for construction and/or as contributions in aid of construction; and (i) in addition to customer growth and developer-funded improvements inflation would reduce the relative impact of further surcharges - if DWR's loan authority is extended.

Construction Required - Staff's Position

The staff brief derides these contentions and asserts that: (a) Phases II and III will never leave the drawing board; (b) "while Phase I does include certain high priority components, it remains a plan within a plan, the engineering and logical efficacy of which are dependent upon the later construction of Phases II and III"; (c) absent meaningful prospects for construction of Phases II and III, it would be folly to approve the application, e.g., the proposed upgrading of applicant's storage and supply capability at a cost of $88,000 is designed for the year 2000 and is unnecessary at this time because

applicant's witness testified that the "supply is currently adequate to meet present demand"; (d) the loan proceeds are directed more towards meeting HD engineering standards than toward abating any health hazard posed by applicant's water supply; (e) HD's witness "testified that potential health threats exist...with respect to pressure inadequacies, potential for contamination through back-siphonage into the system, interruptions in service and outages throughout a good portion of the system"; and (f) full compliance with HD's engineering standards will not be met until Phases II and III are completed and on line.

The staff brief also criticizes applicant's plan because it was not "designed to replace the most unreliable portions of the current distribution system..."

Construction Required - Evidence Rebutting Staff's Position

The registered civil engineer who designed the proposed system testified that: (a) a patchwork of short main replacements would solve operational and maintenance problems but would not provide fire protection to the greatest number of people; (b) a patchwork plan would leave constrictions throughout the various pressure zones preventing water in one zone from being used to reinforce other zones requiring additional water; (c) the Phase I plan is an integrated design which would permit water from applicant's sources of supply to move one way and at the same time storage could be moved downstream to meet system demands; and (d) a patchwork approach would not be desirable even if Phases II and III are never constructed.

An engineering witness for HD testified that:

"With respect to Arrowhead Manor Water Company, the Department of Health Services' findings are that the present system conditions cannot provide a pure, wholesome and potable water at all times.

"This relates to the extremely substandard distribution main lines which are undersized, very shallow, many are very old and in poor condition, subject to freezing, et cetera.

"And these conditions represent a significant potential health threat with respect to pressure inadequacies, potential for contamination through back-siphonage into the system, interruptions in service and outages throughout a good portion of the system.

"Based on these findings, our department recommended strongly to the Arrowhead Manor Water Company that they pursue a loan under the Safe Drinking Water Bond law.

"I'd like to just further mention that the financial report has been reviewed and approved on the project by the Department of Water Resources, and detailed engineering plans and specifications have been reviewed and approved by our department."

He further testified that the Phase I facilities contained the items with the highest priority in the overall improvement plan and that construction of those facilities would be a good step in the right direction.

A DWR witness testified that if HD indicates that a project will substantially bring a system up to standards, DWR could fund the improvement. He would recommend funding of applicant's Phase I plan.

A staff engineer testified that "the new facilities and replacements are needed in order to provide more satisfactory water service" and upon completion of Phase I of "this proposed project, all customers will have an increased level of service, fire service will improve, and customers will experience improvement in water pressure throughout the system."

Customer Support

The staff brief also recommends denial of the application because (a) applicant made no affirmative showing as to customer acceptance of the DWR loan and related surcharges pursuant to the Commission's instruction in D.90877[11/] and to the ALJ's ruling which required applicant to distribute a notice to its customers, Reference Item H, stating that it had decided to reduce the size of its construction program to the initial Phase I revision; (b) the letters received by the staff and customer testimony at the hearing opposed the surcharges; (c) testimony that some 50 persons viewed the construction plans posted at applicant's business office and expressed their approval of the project should be considered in light of the fact that the posted plans did not reveal that Phases II and III probably would not be built before 1990, if at all, or that Phase I, as depicted on the map, was the original larger Phase I; (d) only about one-third of applicant's customers reside in the service area; (e) the remaining customers who maintain a vacation home or rent out their homes occupy their properties for varying

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11/ D.90877 states:

> "If applicant proposes to go forward with its loan application, it should be prepared to discuss the acceptability and willingness of its customers to pay higher proposed surcharges if a larger loan is sought, or to pay the requested surcharge for a substantially reduced construction program at a further hearing in this proceeding."

lengths of time; (f) vacation homeowners who use their cabins for a few weekends a year have little incentive to pay the surcharge; (g) any customer flight could seriously burden the remaining customers who at the outset would be liable for up to $3,500 in rate surcharges over the life of the loan; (h) customer acceptance is more crucial in this case where system improvements are involved compared to a case where the improvement would eliminate a health hazard; (i) in prior DWR loan cases the Commission related surcharges (which were low compared to this proposal) to benefits, but applicant did not quantify direct and indirect benefits in this proceeding; and (j) no inference can be made that a silent customer majority consents to applicant's proposal since most of them would derive little or no advantage from the limited Phase I plan.

Distribution of Reference Item H, described above, applicant's posting of the original and revised maps in its office, and the making of Exhibits 8 and 9 available to its customers, gave applicant's customers ample notice of the scope of the revised proposal. Less than 3 percent of applicant's customers expressed opposition to the scaled-down plan and/or surcharges by letter or by statements at the February 29 hearing. Several times that number of customers looked at the revised plan. While none of these customers voiced approval on the record, customers are rarely enthusiastic over the prospect of a rate increase.

Commissioner Claire Dedrick held a further meeting in Twin Peaks on August 23, 1980, at which 14 customers of the applicant attended. The principal concern of applicant's customers is that they will be required to pay the full surcharge amount, but may ultimately receive only marginal improvement in their water service when the construction work is completed.

Discussion

The testimony on the adequacy of applicant's supplies cited in the staff brief (RT 61) was related only to meeting the system's domestic requirements on that hearing day, not on a peak day. As noted above, the Phase I facilities now proposed will deliver sufficient water to meet domestic and fire-flow requirements from the new facilities without the Phases II and III facilities. However, Phases II and III could not logically be constructed without the Phase I facilities.

Most of the needed peak demand on the system would be for meeting fire flows. Applicant's existing system cannot provide adequate fire flows. Applicant's customers stated there was a need for fire protection to protect against forest fires and to prevent a recurrence of houses burning down due to insufficient fire protection.

The Phase I improvements are intended to provide benefits, described above in the testimony of applicant, DWR, HD, and of the Commission staff engineer, to all of applicant's customers. The combination of new water supplies, additional storage, revamped pressure zones, and larger mains are designed to eliminate current outages and very low pressures (not caused by breaks or major leaks) during periods of heavy system demands. However, we are concerned that these service problems will not be fully remedied for all customers.

After installation of the Phase I facilities, fire flows meeting the current requirements of General Order No. 103 would be available for 180 of applicant's customers. Applicant's remaining customers would receive improved fire protection. (See detail on improved fire protection on pages 9 and 10 above.)

There is agreement that it would be desirable to construct all of the proposed facilities at this time. However, the resultant financial burden on applicant's customers would be excessive. Applicant's Phase I plan is conceptually sound and would benefit all of its customers. A patchwork approach would provide limited benefits and would tend to increase unit costs of construction. There is no need to wait for the contamination of applicant's water supply to determine that there is a hazard. The threat of back-siphonage in an unsewered area is real.

In this instance it is necessary to settle for half a loaf and allow construction of Phase I absent a schedule for the construction of Phases II and III and of replacements of undersized used and useful mains not included in the replacement plan.

There is no argument that construction dates for Phases II and III construction are speculative. However, applicant's consultants are not operating in a vacuum. They have (a) made studies in applicant's service area and in nearby mountain communities; (b) reviewed and reduced population growth projections for applicant's service area made by the San Bernardino County Planning Department; and (c) evaluated the potential for lifting the local building moratorium based on efforts to install a sewer system to serve applicant's service area.

There is a trend for vacationers to cut back on their travel plans and to travel shorter distances on their vacations due to the scarcity and increased cost of fuel.

Applicant's service area is quite close to the cities of San Bernardino and Riverside and is within an easy driving distance from the greater Los Angeles and Orange County metropolitan areas. Due to its location, there will be pressures for further development in the service area.

Applicant contends that in A.49895 it did attempt to secure Commission authorization to make substantial improvements to its system at a fraction of today's costs but that in D.74888 dated October 29, 1968 the Commission did not grant the necessary authority for it to proceed. Finding 2 stated:

> "2. The lack of assured financing for Stage I improvements, coupled with the questionable effectiveness of such improvements, unless sources of water supply are adequate, renders the proposed improvements too uncertain of actual installation and of system benefit for consideration in fixing rates at this time."[12/]

12/ However, the decision indicated that consideration would be given to further rate relief upon applicant's filing a proper showing that it had overcome problem areas associated with the Stage I improvements.

In this proceeding applicant plans to obtain adequate, supplemental sources of supply and storage and to install a system to effectively use those resources with an available long-term, low-cost DWR loan.

The following text in D.74888 is relevant:

> "Some of applicant's present customers feel that they are now paying excessive bills for the short periods in which they occupy their mountain cabins. It should be apparent to them, however, that the water system must be so constructed and maintained that the peak demands on the system may be met. The physical system may not be expanded during periods of high demand and contracted during periods when little water is used, nor can year-round maintenance and repairs be foregone if the system is to continue to serve its customers."

Applicant should consider the advisability of abandoning the smaller dead-end mains on its system which are not used to convey water or to serve customers[13/] to lessen its maintenance problems and water losses. A blowoff valve should be installed at or immediately adjacent to the end of the active main. Future main extensions should be made in accordance with applicant's filed main extension rule.

13/ If service had previously been established to a property not now being served, the abandonment should not preclude re-establishment of that service.

The Hook Creek improvement could not be completed by July 31, 1980. The following procedures must be completed before construction may begin: (a) the DWR loan agreement must be executed; (b) construction drawings must be prepared; (c) construction bids must be solicited and a bid accepted; and (d) necessary survey and right-of-way work must be completed. We will, therefore, extend the completion time for that improvement until December 30, 1980. If possible, applicant should complete all of the Phase I improvements by that date to lessen the inflationary erosion of the loan funds, to possibly construct some of the Phase II improvements, and to provide the benefits of the improvements to its long-suffering customers as soon as possible.

We recognize that the proposed increase in rates exceeds the guidelines for voluntary noninflationary prices promulgated by the President's Council on Wage and Price Stability. The increase, however, is in keeping with the exceptions noted in Section 705-C-B(d) (iii) of the Council's guidelines. That section indicates that exceptions to the guidelines are warranted if, as here, the guidelines would impose extreme hardships and gross inequities on utilities. Circumstances which constitute a hardship include inadequate cash flow. Under existing rates applicant would not have sufficient cash flow to meet the principal and interest payments on the proposed loan from DWR. The rate surcharge, therefore, is in accordance with the guideline exceptions of the President's Council on Wage and Price Stability.

The DWR loan repayment surcharge should be separately identified on customer bills. The utility plant financed through the surcharge should be permanently excluded from rate base for ratemaking purposes and the depreciation on this plant should be recorded in memorandum accounts, for income tax purposes only.

Applicant should establish a balancing account to be credited with revenue collected through the surcharge and with investment tax credits arising from the plant reconstruction program as they are utilized. The balancing account should be charged with payments of interest and principal on the loan. The surcharge should be adjusted periodically to reflect changes in the number and type of connections and larger meters, and resulting overages or shortages in the balancing account.

Future changes in such rates should be accomplished by normal advice letter procedures.

We emphasize that the surcharge authorized herein will cover only the cost of the loan incurred to finance the added plant, not any additional operating expenses that may be incurred. It may not preclude future rate increase requests to cover additional costs of repair materials, wages, property taxes, power bills, operation of the treatment plant, or other operating expenses.

We also place applicant on notice that it is our intent to review the surcharge amount in applicant's next general rate increase proceeding to determine whether the surcharge amount should be reduced for those customers receiving only marginal improvement in water service after the construction work authorized herein is completed.

For the surcharge to produce enough revenue to meet the initial payment of interest and principal on the DWR loan, it is necessary for applicant to place the surcharge in effect in advance to enable it to initially accumulate a small surplus in its balancing account to compensate for the time lag between billing and collection dates and, if future surcharges are based on water use, for errors in estimating water use. Applicant should file an advice letter setting forth its construction scheduling, anticipated loan drawdowns, dates for making its loan payments, its proposed scheduling for placing the surcharge in effect, and the frequency and amount of the proration of the annual billings. We may then issue a resolution authorizing applicant to file a prorated billing surcharge rate schedule.

Findings of Fact

1. Applicant's system requires greater transmission capacity, additional storage, and sources of supply to meet the needs of its customers.

2. The funds from the DWR loan are needed to construct Phase I of a three-phase improvement plan, which will (a) provide an adequately sized backbone transmission system; (b) eliminate or improve low pressure conditions; (c) provide an adequate water supply and storage to meet the needs of its existing customers and to provide a margin for growth; (d) provide water to meet direct fire protection requirements adjacent to the new facilities and

the heavily forested service areas; (e) improve fire protection in areas not directly accessible to the new facilities; (f) eliminate some potential backflow hazards, including replacement of the badly deteriorated portion of a main on Hook Creek Road; and (g) provide the core of facilities needed for Phases II and III.

3. The facilities proposed to be constructed with the loan funds constitute only a portion of the mains, services, fire hydrants, and meters originally proposed to be constructed with the proceeds of the requested loan.

4. Applicant's operating funds have only sufficed to patch leaks or to replace short sections of undersized mains.

5. Applicant's customers received adequate notice of the original and revised scope and cost of the proposed construction plan and of the surcharges required to amortize the DWR loan.

6. Applicant's revised Phase I of its three-phase plan is shown in Exhibits 8-1 and 8-2 herein in response to FPD's suggestions to improve the system's usefulness for fire protection purposes. This latest change dropped the number of customers directly connected to new mains from 159 to 125. Applicant also increased main sizes in the Phase I backbone system.

7. The Phase I facilities as proposed will deliver sufficient water to meet domestic and fire-flow requirements from the new facilities without the Phases II and III facilities.

8. The construction dates for Phases II and III are speculative. There are existing and continuing pressures to further develop this resort area located in close proximity to major metropolitan areas.

9. A building moratorium exists because of the lack of sewers in the service area. Efforts are under way to secure support for a sewer improvement district to cure this deficiency and lift the moratorium.

10. Certain procedural requirements must be completed before construction can be commenced. It is uncertain if the badly deteriorated and leaking Hook Creek Road main replacement ordered in D.90877 can be completed by July 31, 1980. This improvement is a portion of the main construction on Hook Creek Road included in Phase I.

11. The proposed water system improvements are needed to produce a healthful, reliable water supply.

12. The proposed borrowing is for proper purposes, and the money, property, or labor to be procured or paid for by the issue of the loan authorized by this decision is reasonably required for the purposes specified, which purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

13. A rate surcharge should be established which provides in each six-month period an amount of revenue approximately equal to the periodic loan payment. This surcharge should produce about $5,391 per month, resulting in an increase in water rates of approximately $9.08 per month for a typical residential customer. This rate increase will increase applicant's annual gross revenues by approximately $64,690 per year.

14. The rate surcharge which is established to repay the DWR loan should last as long as the loan. The surcharge should not be intermingled with other utility charges.

15. The utility plant financed through this DWR loan should be permanently excluded from rate base as the customers should not be required to pay more than once for the utility plant.

16. Special accounting requirements are necessary to ensure that there are no unintended windfalls to the utility owners. Applicant should establish a balancing account to be credited with revenue collected through the surcharge, and with investment tax credits resulting from the plant construction, as they are utilized. The balancing account should be reduced by payments of principal and interest on the loan. The surcharge should be adjusted periodically to reflect changes in the number, size, and type of connections (and, possibly in the future, water use) and resulting overages or shortages in the balancing account.

17. The increases in rates and charges authorized by this decision are justified and are reasonable; and the present rates and charges, insofar as they differ from those prescribed by this decision, are for the future unjust and unreasonable.

18. The surcharge should be placed in effect to accumulate funds to make the initial interest, principal, and reserve payment on the DWR loan. The effective date of and amounts of the loan surcharges will be established by Commission resolution after applicant files an advice letter setting forth its construction scheduling, anticipated loan drawdowns, dates for making its loan payments, its proposed scheduling for placing the surcharge in effect, and the frequency and amount of the proration of the annual billings.

19. The proposed surcharge will generate approximately $64,691 per year. Approximately $58,896 will be used to meet the loan payments. The remaining $5,890, which is 10 percent of the loan payment, will be deposited with the fiscal agent in order to accumulate a reserve equal to two semiannual loan payments over a 10-year period.

20. The establishment of a reserve equal to two semiannual loan payments is required by DWR Administrative Regulations.

Conclusions of Law

1. An extension of time to September 30, 1980 should be authorized to permit applicant to complete the Hook Creek Road improvement ordered in D.90877 and to avoid a rate reduction.

2. No further polling of the attitudes of applicant's customers in regard to applicant's request is required.

3. Applicant should be authorized to enter into a loan agreement for $910,520 with DWR on the basis described herein.

4. The rate surcharges set forth in Appendix A attached herein should be authorized. The initial billing date and pro rata rate surcharges should be authorized by Commission resolution as described in Finding 18 herein.

5. The effective date of this order, except for the filing of the fee prescribed by Section 1904(b) of the Public Utilities Code, should be the date hereof to permit applicant to expeditiously utilize the limited remaining portion of the construction season ending on September 30, 1980.

O R D E R

IT IS ORDERED that:

1. Arrowhead Manor Water Company, Inc. (applicant) is authorized to file an advice letter as described in Finding 18 herein. A Commission resolution shall establish the filing date of a prorated rate surcharge schedule based upon the revised annual rate schedule attached to this order as Appendix A. Such filing shall comply with General Order No. 96-A and shall apply only to the service rendered on or after the effective date authorized in that resolution.

2. Applicant is authorized to borrow $910,520 from the State of California, to execute the proposed loan contract, and to use the proceeds as specified in the application, as amended.

3. As a condition of the rate increase granted herein, applicant shall be responsible for refunding or applying on behalf of customers any surplus accrued in the balancing account when ordered by the Commission.

4. Applicant shall establish and maintain a separate balancing account which shall include all billed surcharge revenue and the value of investment tax credits on the plant, as utilized. The balancing account shall be reduced by payments of principal and interest to the State Department of Water Resources (DWR). A separate statement pertaining to the surcharge shall appear on each customer's water bill issued by applicant.

5. Plant financed through the DWR loan shall be permanently excluded from rate base.

6. The last sentence of Ordering Paragraph 2 of Decision No. 90877 is revised as follows:

> This rate increase shall be rescinded on October 1, 1980 if the Hook Creek Road improvement has not been completed by September 30, 1980.

The authority granted by this order to issue an evidence of indebtedness and to execute a loan contract will become effective when applicant has paid the fee prescribed by Section 1904(b) of the Public Utilities Code, which fee is $1,822. In all other respects the effective date of this order is the date hereof.

Dated SEP 3 - 1980, at San Francisco, California.

President

Commissioners

PUBLIC UTILITIES COMMISSION
STATE OF CALIFORNIA
101570
SEP 17 1980
1,822.-
By

A.57533

APPENDIX A
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ARROWHEAD MANOR WATER CO., INC.

Schedule No. 1A

ANNUAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service furnished on an annual basis.

TERRITORY

The unincorporated community of Cedar Glen and vicinity, located approximately one mile southeast of Lake Arrowhead, San Bernardino County.

RATES

Annual Quantity Rates:	Per Meter Per Year
First 3,600 cu.ft., per 100 cu.ft.	$ .60
Over 3,600 cu.ft., per 100 cu.ft.	.70

Annual Service Charges:	Per Service Connection		
	Annual Charge	Annual Surcharge	
For 5/8 x 3/4-inch meter	$ 72.50	$109.00	(N)
For 3/4-inch meter	80.00	163.50	↓
For 1-inch meter	110.00	272.50	↓
For 1½-inch meter	147.50	545.00	↓
For 2-inch meter	200.00	872.00	(N)

The Service Charge is applicable to all metered service. It is a readiness-to-serve charge to which is added the charge, computed at the Quantity Rates, for water used during the year.

METERED SERVICE SURCHARGE

NOTE: This surcharge is in addition to the regular annual metered water bill. The total annual surcharge must be identified on each bill. This surcharge is specifically for the repayment of the California Safe Drinking Water Bond Act loan authorized by Decision No. (a). (N)

(a) Insert Decision Number in Application No. 57533 before filing tariff. (N)

Schedule No. 1A

ANNUAL METERED SERVICE (Continued)

SPECIAL CONDITIONS

1. The annual service charge applies to service during the 12-month period commencing January 1 and is due in advance. If a permanent resident of the area has been a customer of the utility for at least 12 months, he may elect, at the beginning of the calendar year, to pay prorated minimum charges in advance at intervals of less than one year (monthly, bimonthly, or quarterly) in accordance with the utility's established billing periods for water used in excess of the monthly allowance under the annual service charge. When meters are read bimonthly or quarterly, the charge will be computed by doubling or tripling, respectively, the number of cubic feet to which each block rate is applicable on a monthly basis except that meters may be read and quantity charges billed during the winter season at intervals greater than three months.

2. The opening bill for metered service, except upon conversion from flat rate service, shall be the established annual service charge for the service. Where initial service is established after the first day of any year, the portion of such annual charge applicable to the current year shall be determined by multiplying the annual charge by one three-hundred-sixty-fifth (1/365) of the number of days remaining in the calendar year. The balance of the payment of the initial annual charge shall be credited against the charges for the succeeding annual period. If service is not continued for at least one year after the date of initial service, no refund of the initial annual charge shall be due the customer.

Schedule No. 2RA

ANNUAL RESIDENTIAL FLAT RATE SERVICE

APPLICABILITY

Applicable to all flat rate residential water service furnished on an annual basis.

TERRITORY

The unincorporated community of Cedar Glen and vicinity, located approximately one mile southeast of Lake Arrowhead, San Bernardino County.

RATES	Per Service Connection Per Year		
	Charge	Surcharge	
For a single-family residential unit, including premises	$92.50	$109.00	(N)
For each additional single-family residential unit on the same premises and served from the same service connection	62.50	73.65	(N)

FLAT RATE SERVICE SURCHARGE

NOTE: This surcharge is in addition to the regular charge of $92.50 per one inch or less service connection, per year. The total surcharge is specifically for the repayment of the California Safe Drinking Water Bond Act loan as authorized by Decision No. ____(a)____.

(a) Insert Decision Number in Application No. 57533 before filing tariff.

Schedule No. 2RA

ANNUAL RESIDENTIAL FLAT RATE SERVICE (continued)

SPECIAL CONDITIONS

1. The above flat rate and surcharge applies to a service connection not larger than one inch in diameter. (T)

2. For service covered by the above classification, if the utility so elects, a meter shall be installed and service provided under Schedule No. 1A, Annual Metered Service, effective as of the first day of the following calendar month. Where the flat rate charge for a period has been paid in advance, refund of the prorated difference between such flat rate payment and the meter service charge for the same period shall be made on or before that day. (T)

3. The annual flat rate charge applies to service during the 12-month period commencing January 1 and is due in advance. If a permanent resident of the area has been a customer of the utility for at least 12 months, he may elect, at the beginning of the calendar year, to pay prorated flat rate charges and annual surcharge in advance at intervals of less than one year (monthly, bimonthly, or quarterly) in accordance with the utility's established billing periods. A nonpermanent resident may elect to pay the annual charge and annual surcharge in two equal installments. Where such a resident has failed to pay the first half of the annual charge and surcharge due January 1, service will not be restored until the total annual charge and surcharge has been paid. (T)

4. The opening bill for flat rate service shall be the established annual flat rate charge and surcharge for the service. Where initial service is established after the first day of any year, the portion of such annual charge and surcharge applicable to the current year shall be determined by multiplying the annual charge and surcharge by one three-hundred-sixty-fifth (1/365) of the number of days remaining in the calendar year. The balance of the payment of the initial annual charge and surcharge shall be credited against the charges for the succeeding annual period. If service is not continued for at least one year after the date of initial service, no refund of the initial annual charges shall be due the customer. (T)